BEFORE THE

Federal Communications Commission

WASHINGTON, D.C.

In the Matter of	)	
	)	
Accounting for Judgments	)	CC Docket No. 93-240
and Other Costs Associated	)	
with Litigation	)	

COMMENTS OF COMSAT CORPORATION

Philip L. Verveer
John L. McGrew
Francis M. Buono

Willkie Farr & Gallagher
Three Lafayette Centre
1155 21st Street, N.W.
Suite 600
Washington, D.C. 20036-3384

Its Attorneys

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SUMMARY

The Commission's proposal to establish the outcome of the antitrust suit as the litmus test for triggering below-the-line treatment of antitrust judgments, settlements, and litigation expenses constitutes a dramatic departure from the traditional ad hoc approach, which presumes good faith on the part of the regulated carriers, while providing for the disallowance of expenses which are demonstrably exorbitant, unnecessary, wasteful, or otherwise imprudent. This time-tested approach strikes the optimal balance between carrier and ratepayer interests, and the Commission has provided no reasoned analysis justifying its proposed radical departure from it.

Moreover, the Commission's proposed outcome-dependent approach, with its myopic focus on the technical "success" or "failure" of the litigation, will create perverse economic incentives that serve to deter efficient pro-competitive behavior by regulated carriers. Given the increasingly complex landscape of antitrust jurisprudence, in which a very fine line distinguishes aggressive, pro-competitive behavior from behavior which may be viewed as constituting an antitrust violation, a blanket presumption of cost disallowance based solely on the outcome of the litigation inevitably will have a substantial chilling effect on carriers' incentives to engage in vigorous competition (to the benefit of consumers) up to the limits imposed by the antitrust laws. In many instances, the proposed rules will have a real-world impact that is directly contrary to

the "ratepayer benefit" principle which the rules purport to serve.

With respect to the Notice's specific proposals, COMSAT responds as follows:

- The fact that the overwhelming majority of antitrust suits result in settlement rather than adverse judgments reflects the fine line between vigorous competition and activities that may be viewed as an antitrust violation, and underscores the need for careful consideration of the impact of the Commission's proposal on carrier incentives.

- The Commission's proposal is based, in large part, on an erroneous assumption that suits are settled because a carrier believes it is likely to lose the case and ignores the myriad of other factors that are involved in a decision to settle.

- The Commission's presumptive disallowance of settlements ignores the fact that settlements frequently benefit ratepayers and other consumers by putting an end to expensive and often protracted litigation.

- Subjecting antitrust settlements at any stage to an adverse presumption of disallowance will discourage the settlement of antitrust cases and, as such, would (1) directly contravene longstanding judicial and congressional policy favoring compromise; and (2) have a further chilling effect on otherwise pro-competitive behavior.

- The Commission's proposal to limit above-the-line treatment of pre-judgment settlements to nuisance value is at odds with the Commission's fundamental premise (which is itself flawed), namely that "it is the entry of a court decision that a law has been violated that drives our treatment of these costs."

- The Commission's distinction between pre- and post-judgment settlements creates excessive incentives (1) to continue to litigate after an adverse judgment and (2) to settle prior to judgment.

- The Commission's proposed treatment of antitrust litigation expenses must be rejected based on the Litton Accounting Appeal's legal and policy analyses.

- Use of a balance sheet deferral account for litigation expenses is unworkable and inappropriate as a matter of public policy. Such an approach would unfairly deprive carriers of the opportunity to recoup prudently incurred litigation expenses for what may be a significant period, even where the carrier's conduct ultimately is found to be wholly within the law.

- The Commission's proposed extension of its rules to areas beyond the antitrust context, as well as its attempt to impose interim accounting requirements on carriers, are wholly insupportable.

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COMSAT Corporation ("COMSAT") hereby submits the following comments in response to the Commission's Notice of Proposed Rulemaking in the above-captioned proceeding.[1]

I. THE COMMISSION HAS FAILED TO PROVIDE A REASONED EXPLANATION FOR ITS PROPOSED RADICAL DEPARTURE FROM LONGSTANDING ACCOUNTING RULES AND RATEMAKING POLICIES

It has long been a fundamental principle of public utility ratemaking that a regulated carrier is entitled to recover through its rates all costs and expenses prudently incurred in the course of operating the regulated business.[2] "Good faith is

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[1] Accounting for Judgments and Other Costs Associated with Litigation, Notice of Proposed Rulemaking, CC Docket No. 93-240, FCC 93-424 (released September 9, 1993) ("Notice").

[2] See, e.g., State of Missouri v. Public Service Commission, 262 U.S. 276, 289 n.1 (1923); West Ohio Gas Co. v. Public Utilities Commission, 294 U.S. 63, 72 (1935).

to be presumed on the part of the managers of a business," the Supreme Court has declared.[3] In fact, the Commission itself has previously acknowledged the efficacy of this time-tested prudence standard:

> While the [FCC] regulates rates, it does not manage the carrier's business. Good faith is presumed on the part of the carrier's management, and it has been stated that public utility commissions should not substitute their judgments as to the reasonableness of expenses in the absence of a showing of inefficiency or improvidence.... They may disallow expenses actually incurred in the company's operation where the challenged expense is found to be exorbitant, unnecessary, wasteful, extravagant, or incurred in the abuse of discretion or bad faith, or of a non-recurring nature.[4]

In contrast, the Commission's proposed accounting rules and ratemaking policies for litigation costs have nothing to do with whether these litigation expenses are prudently incurred.[5] Rather, they are based exclusively on whether "a court has determined that a carrier has violated a federal law."[6] The

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[3] West Ohio Gas, 294 U.S. at 72.

[4] Policy to be Followed in the Allowance of Litigation Expenses of Common Carriers in Ratemaking Proceedings, 92 F.C.C.2d 140, 144 ¶ 9 (citing State of Missouri and West Ohio Gas, supra, n.2) ("Policy Decision"). See also AT&T Charges for Interstate Telephone Service, 64 F.C.C.2d 1, 85-86 (1977); COMSAT Investigation into Charges, Practices, Classifications, Rates, and Regulations, 56 F.C.C.2d 1101, 1174-75 (1975).

[5] Obviously, the decision to pay a judgment of a court is more than simply a matter of prudence. But even here, as the Commission's proposed rules sweep the entire body of antitrust law into a single adverse presumption, all consideration of reasonableness and prudence are, as a practical matter, eliminated.

[6] Accounting for Judgments and Other Costs Associated with Antitrust Lawsuits, Order on Reconsideration, 4 FCC Rcd. (continued...)

Commission announces the adoption of a new "guiding principle," namely a sweeping and, as will be seen, flawed presumption that "certain litigation costs [are] not 'normally the byproduct of activities that benefit ratepayers.'"[7] Further, to implement this novel principle, the Commission proposes new accounting rules and ratemaking policies which abandon the longstanding prudence standard and look instead solely to the "success" or "failure" of the carrier in defending against the antitrust (or other federal) suit.[8]

As discussed below, the traditional, ad hoc approach strikes the optimal balance between carrier and ratepayer interests, and the Commission has failed to provide a coherent legal or policy justification for its new guiding principle or for its outcome-dependent implementing standard. Accordingly, COMSAT recommends that rather than establishing an absolute rule of presumptive disallowance, the Commission should continue its longstanding practice of presuming that litigation costs are incurred in the normal course of business and disallowing these costs in

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[6](...continued)
4092, 4094 ¶ 18 (1989), vacated, Mountain States Telephone and Telegraph Co. v. F.C.C., 939 F.2d 1035 (1991).

[7] Notice at ¶ 3 (internal citation omitted).

[8] See Accounting for Judgments and Other Costs Associated with Antitrust Lawsuits, Notice of Proposed Rulemaking, CC Docket No. 85-64, FCC 85-120 (released May 3, 1985) at ¶ 8 ("The linchpin for the accounting treatment is the finding of guilty, that is, the establishment at trial (or by the defendant's admission) of a violation of the antitrust laws").

individual rate cases only when there is clear evidence of management imprudence or bad faith.

A. After Thorough Legal and Policy Analyses, the Litton Accounting Appeal Properly Found that the Commission Had Not Adequately Justified a Radical Departure From Longstanding Accounting and Ratemaking Policies

In the Litton Accounting Appeal, the D.C. Court of Appeals undertook a thorough legal and policy analysis of the Commission's earlier attempt to depart from its traditional accounting and ratemaking treatment of litigation expenses and concluded in both instances that the Commission failed to justify its new approach.[9] Central to the Court's criticism was the Commission's establishment of the carrier's "success" or "failure" in the antitrust litigation as the sole determinant of the presumptive allowance or disallowance of litigation expenses. As a legal matter, the Court concluded:

> We are thus not persuaded that the Commission's legal rationale for its broad position finds a safe haven in the caselaw. The Commission makes clear that an adjudicated antitrust violation, standing alone, will invariably trigger its accounting directive and the accompanying presumption, but pertinent decisions convince us that logic and reasonableness require a wider and more discriminating focus.[10]

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[9] Although the Litton Court focused primarily on the propriety of the Commission's rules regarding litigation expenses, its overarching legal and policy analyses, particularly its criticism of the Commission's failure to advance a reasoned analysis justifying its proposed radical departure from longstanding precedent, apply with equal force to the Notice's proposals regarding antitrust judgments and settlements.

[10] Mountain States Telephone and Telegraph Co. v. F.C.C., 939 F.2d 1021, 1033 (D.C. Cir. 1991) (emphasis added) ("Litton Accounting Appeal" or "Litton Court").

The Court also found that the Commission's treatment of litigation expenses was equally unsupported by any policy rationale:

> Is the Commission saying that the new procedure, with below-the-line movement of antitrust litigation expenses and an adverse presumption, better "strikes the proper balance" between utility and consumer than does the time-tested traditional procedure featuring above-the-line accounting and a burden of justification only upon challenge, which only two years previously the Commission had probed deeply and found adequate? If the new procedure is superior, how so; if not, why the change? We are left equally in the dark by the Commission's reference to justification "on equity or other public interest grounds." This terminology is much too general to provide any real insight, and the Commission does not elucidate.[11]

In short, the Litton Court's analyses found that "the tension between longstanding judicial and newly devised administrative procedures could hardly be more severe," and that "the Commission's expositions of its underlying reasoning [is] 'intolerably mute.'"[12] Accordingly, the Court vacated the Commission's order and remanded the case to the agency with instructions to provide a "reasoned explanation for any failure to adhere to its own precedents."[13] This explanation must establish a "rational connection between the facts found and the

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[11] Id. at 1034 (internal citations omitted).

[12] Id. at 1034-35 (internal citations omitted).

[13] Id. at 1035 (internal citations omitted).

choice made" and must be "articulated with sufficient clarity or specificity to permit a court to engage in meaningful review."[14]

As the following section discusses, the accounting rules proposed by the Notice still suffer from the fundamental defect of lacking a reasoned connection between the "ratepayer benefit" principle the Commission seeks to implement and the outcome-dependent standard by which the Commission proposes to implement it.

B. The Litigation Costs Decision's Affirmance of the Ratepayer Benefit Principle is Irrelevant, Since the Proposed Method of Implementing This Principle is Fundamentally Flawed

The sole rationale advanced by the Notice in support of the new accounting rules and ratemaking policies is the Litigation Costs Decision's affirmance of the Commission's "ratepayer benefit" principle.[15] The Court's affirmance of this principle, however, is irrelevant. What is relevant is the fact that the Commission's success-failure standard used to determine whether ratepayers have been benefitted is based on a fundamentally unsound blanket presumption that litigation expenses are

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[14] Id. The Commission's recent termination of the Litton proceeding, see Accounting Instructions for the Judgment and Other Costs Associated with the Litton Systems Antitrust Lawsuit, Order on Remand, FCC 93-431 (released September 27, 1993), in no way diminishes the relevance of the Litton Court's analyses to the instant proceeding.

[15] See, e.g., Notice at ¶¶ 9,11,16 (citing Mountain States Telephone and Telegraph Co. v. F.C.C., 939 F.2d 1035, 1043-47 (D.C. Cir. 1991) ("Litigation Costs Decision").

unnecessary, imprudent, and unreasonable whenever a carrier loses an antitrust suit. As the Litton Court concluded, however:

> Illegality of carrier conduct from which an antitrust litigation expense stems does not inexorably compel or warrant either rejection or stigmatization of the expense as a factor in rate calculations.[16]

Rather, as the Court continued, "a pervasive element in ratemaking is reasonableness, which demands inquiry beyond the bare fact of antitrust violation."[17] Indeed, one can envision alternative methods for implementing a ratepayer benefit principle which rely on a wider and more discriminating focus than the Commission's outcome-dependent approach.

One such alternative approach is illustrated by Appalachian Electric Power Co. v. F.P.C., 218 F.2d 773 (4th Cir. 1955), in which the court held that the costs of litigation incurred by a regulatee to determine the necessity of obtaining a license should be included in rate calculations, notwithstanding the fact that the regulatee lost the suit. Of particular note is the court's finding that a determination of whether ratepayers were benefitted requires an analysis beyond the mere outcome of the litigation into the reasonableness of the costs incurred.[18]

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[16] Litton Accounting Appeal, 939 F.2d at 1031.

[17] Id. (emphasis added).

[18] 218 F.2d at 777. As the Litton Court also explained, the Supreme Court, in the closely analogous field of taxation, has rejected the use of a success-failure standard for determining the deductibility of litigation expenses. Litton Accounting Appeal, 939 F.2d at 1031-33 (citing Commissioner v. Heininger, 320 U.S. 467 (1943) and Commissioner v. Tellier, 383 U.S. 687 (1966)).

Thus, in relying almost exclusively on the Litigation Costs Decision's affirmance of its ratepayer benefit principle and completely rejecting the Litton Court's criticisms, the Commission overlooks the more fundamental problem inherent in its proposed accounting and ratemaking approach, namely the establishment of the "success" or "failure" of the lawsuit as the sole determinant of whether allowance or disallowance of the carrier's litigation expenses will be presumed. In the end, this unwavering focus on the outcome of the litigation renders the Commission's entire scheme invalid. In addition, as discussed in the next section, this outcome-dependent approach is inappropriate as a matter of policy due to the substantial perverse incentives it will create.

II. THE BROAD PRESUMPTION OF DISALLOWANCE WHICH UNDERLIES THE COMMISSION'S PROPOSED ACCOUNTING RULES AND RATEMAKING POLICIES HAS NO VALID BASIS IN FACT, LAW, OR SOUND PUBLIC POLICY

A. Adoption of the Commission's Antitrust Litigation Cost Rules Would Give Rise to Perverse Economic Incentives that Serve to Deter Efficient Pro-Competitive Behavior By Regulated Carriers

As the foregoing discussion demonstrates, the Commission's proposals for presumptive below-the-line treatment of antitrust litigation costs constitute a radical departure from its past practice, and the Commission has provided no "authority either mandating or unequivocally authorizing [this] singular accounting prescription or presumption."[19]

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[19] Litton Accounting Appeal, 939 F.2d at 1030.

Indeed, it is difficult to imagine a rational justification for the approach proposed by the Notice. A strong presumption of disallowance for a particular type of expense would be appropriate only if the nature of the expense is such that it would virtually always result from imprudence. Such is not the case for antitrust-related expenses which, in today's highly litigious society, are normal, ordinary, and recurring costs of operating the carrier's business.[20]

Given the myriad uncertainties and the ever-changing standards applied by the courts in the antitrust context, business decisions which may have been entirely reasonable, prudent, and very much lawful under prevailing precedents at the time they were made subsequently may be challenged under evolving antitrust jurisprudence and a rapidly changing industry structure. Moreover, in considering claims involving alleged violations of the antitrust laws, courts have universally observed that a very fine line divides vigorous competition (which the Commission presumably wishes to promote) and behavior

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[20] In addition, the Commission's proposal to treat such costs as extraordinary items is contrary to GAAP (under which extraordinary items must be unusual in nature, taking into consideration the environment in which the enterprise operates, and must not be expected to occur frequently) and with the IRS' treatment of them as ordinary and necessary business expenses that are fully deductible. See footnote 18, supra.

which may be viewed as constituting an antitrust violation.[21] As one oft-quoted opinion has aptly described it:

> Competition is a ruthless process. A firm that reduces cost and expands sales injures rivals -- sometimes fatally. The firm that slashes costs the most captures the greatest sales and inflicts the greatest injury. The deeper the injury to rivals, the greater the potential benefit. These injuries to rivals are byproducts of vigorous competition, and the antitrust laws are not balm for rivals' wounds. The antitrust laws are for the benefit of competition, not competitors.... Action that injures rivals may ultimately injure consumers, but it is also perfectly consistent with competition, and to deter aggressive conduct is to deter competition.... "It is not enough that a single firm appears to 'restrain trade' unreasonably, for even a vigorous competitor may leave that impression...."[22]

In this context, a blanket presumption of cost disallowance inevitably will have a substantial chilling effect on carriers' incentives to engage in vigorous competition (to the benefit of consumers) up to the limits imposed by the antitrust laws.[23] As

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[21] See, e.g., Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 116 (1986) ("[C]ompetition for increased market share, is not activity forbidden by the antitrust laws. It is simply, as petitioners claim, vigorous competition.... 'It is in the interest of competition to permit dominant firms to engage in vigorous competition, including price competition'") (internal citations omitted).

[22] Ball Memorial Hospital, Inc. v. Mutual Hosp. Ins., 784 F.2d 1325, 1338, reh'g denied, 788 F.2d 1223 (7th Cir. 1986) (internal citations omitted) (first emphasis in original; second emphasis added).

[23] See Matsushita Electric Industrial Co. v. Zenith Radio Corp., 475 U.S. 574, 594 (1986) ("[C]ourts should not permit factfinders to infer conspiracies when such inferences are implausible, because the effect of such practices is often to deter pro-competitive conduct.... [C]utting prices in order to increase business often is the very essence of competition. Thus, mistaken inferences in cases such as this one are especially costly, because they chill the very conduct the

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the Litigation Costs Decision described it, the Commission's rules may well create "perverse carrier incentives" which will cause a carrier to be "overly conservative in its decisions concerning activities that are very likely to benefit ratepayers but might conceivably be found to violate federal law."[24] Seen in this light, the Commission's single-minded, outcome-oriented approach will, in many cases, "cause an increase in the costs to be borne by ratepayers,"[25] as well as other consumers.

For example, the Commission's presumptive disallowance of all adverse antitrust judgments ignores the complexity of antitrust suits. Often, there is no clear winner and loser in these cases. If a carrier is sued for a large amount, defends, and judgment is entered for a small amount, most would consider the defense a "success," although it may be technically deemed a "failure." Moreover, as the Court of Appeals has recognized, even where some liability is found, the behavior which gave rise to the "adverse" judgment may in fact have redounded to the benefit of the carriers' ratepayers.[26] The Commission's approach does not account for these inherent complexities and subtleties, however, linking as it does the presumptive disallowance of

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[23](...continued)
antitrust laws are designed to protect"); Monsanto Co. v. Spray-rite Service Corp., 465 U.S. 752, 762-64, reh'g denied, 466 U.S. 994 (1984) (same).

[24] Litigation Costs Decision, 939 F.2d at 1046.

[25] Id. at 1047 (emphasis added).

[26] Id. at 1043, 1046-47.

litigation costs solely to the outcome of the suit. The better approach, and the one more consonant with the practical realities and complexities of antitrust suits, is for such costs to be recorded in operating accounts, and for the Commission to adhere to its traditional approach of reviewing the various accounts to determine whether the carrier's underlying business decisions were reasonable and making any necessary disallowances of above-the-line costs on an ad hoc basis during a ratemaking proceeding. As the discussion below indicates, the wisdom of maintaining this time-tested approach is even more apparent when one considers the potential adverse effects of the Commission's proposed rules with respect to antitrust settlements and other litigation-related expenses.[27]

Nor is it an adequate response for the Commission to cite the carrier's ability "to argue, in the ratemaking process, that a particular [expense] should be included in its revenue requirement."[28] It is unrealistic to think that once a cost is assigned below the line, it will be moved into a carrier's revenue requirement during a rate proceeding. The Commission's outcome-determinative adverse presumption creates a difficult, if not impossible, burden to overcome.[29]

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[27] See discussion of settlements at 13-20, infra and the discussion of other litigation expenses at 20-24, infra.

[28] See Notice at ¶ 10.

[29] See Litton Accounting Appeal, 939 F.2d at 1030.

B. The Proposed Treatment of Antitrust Settlements Creates Artificial Incentives Which Will Have Adverse Effects on Ratepayers and Other Consumers

1. The Commission's Proposed Treatment of Settlements Conflicts with Longstanding Judicial and Congressional Policies and Will Create Perverse Economic Incentives

It is well-established that the overwhelming majority of antitrust suits result in settlement or dismissal rather than adverse judgment.[30] This high percentage of settlements reflects the fine line between vigorous competition and activities that may be viewed as an antitrust violation. It also underscores the need for careful consideration of the impact which the Commission's proposed rules will have on carrier incentives. Unfortunately, as described below, the Commission's proposed accounting and ratemaking treatment for settlements will create perverse economic incentives which will adversely affect ratepayers and other consumers.

The Commission proposes to require carriers to record antitrust settlements below the line because "this approach is most consistent with the underlying principle that expenses not incurred for the benefit of ratepayers should not be routinely

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[30] See, e.g., "Contribution and Claim Reduction in Antitrust Litigation," ABA Sec. Antitrust L. Monograph No. 11, at 32 (over 90% of antitrust treble damages actions settle prior to trial); Salop and White, "Economic Analysis of Private Antitrust Litigation," 74 Geo. L. J. 1001, 1024, 1049-50 (April 1986) (of the 1000 plus private antitrust actions filed each year, as many as 97% result in settlement or dismissal); Kalinowski, "Antitrust Laws and Trade Regulation," vol. IX, § 96.01 (1992) (the Antitrust Division of the Department of Justice has settled in excess of 70% of the cases it has investigated in recent years).

passed on to ratepayers."[31] There are several problems with this proposed accounting approach. First, nowhere does the Commission justify its presumption that settlement costs constitute "expenses not incurred for the benefit of ratepayers." To the contrary, a settlement frequently benefits ratepayers by putting an end to expensive and often protracted litigation. Many times, settlements emerge once it becomes clear in discovery that a plaintiff lacks any factual support for antitrust violations it may have alleged, and it benefits both parties, as well as ratepayers, to cease the fight.

Second, the Commission's proposal is based, in large part, on an erroneous assumption that suits are settled because a carrier believes it is likely to lose the case.[32] Such an assumption has absolutely no basis in law or in fact. The settlement decision typically is the result of a careful weighing of many factors including pressure applied to both sides by the court, the cost of continued litigation, and the need to remove uncertainty and normalize business relations. In law and in fact, the decision to settle does not equate to an admission or a finding of liability on the part of the defendant and thus

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[31] Notice at ¶ 11.

[32] See, e.g., Accounting for Judgments and Other Costs Associated with Antitrust Lawsuits, Notice of Proposed Rulemaking, CC Docket No. 85-64, FCC 85-120 (released May 3, 1985) at ¶ 9 ("[M]ost [antitrust defendants] settle under the real specter of the consequences of losing the case").

provides no basis for a presumption of cost disallowance based (however unreasonably) on such a finding.[33]

Third, subjecting antitrust settlements at any stage to an adverse presumption of disallowance will discourage the settlement of antitrust cases and, as such, would not only directly contravene longstanding judicial and congressional policy which favors compromise to avoid wasteful litigation and associated expenses,[34] but would also have a further chilling effect on otherwise pro-competitive behavior. The proposed

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[33] Well-established judicial and congressional policy soundly rejects any likening of negotiated settlements to admissions of wrongdoing. See, e.g., Fed. R. Evid. 408; Allstate Ins. Co. v. Winnemore, 413 F.2d 858, 863 n.10 (5th Cir. 1969).

The Commission has previously stated that its desire to have prejudgment settlements recorded in a nonoperating account is "not grounded upon a desire to impute wrongdoing in the dispute but rather to make clear that the expenditure will not be considered an ordinary expense for ratemaking purposes, absent further justification." Accounting for Judgments and Other Costs Associated with Antitrust Lawsuits, Report and Order, 2 FCC Rcd. 3241, 3245 ¶ 26 (1987), vacated, Mountain Telephone and Telegraph Co. v. F.C.C., 939 F.2d 1035 (D.C. Cir. 1991) ("Litigation Costs Order"). However, the Commission's statement is at best tautological. Clearly, recordation in a nonoperating account will signify that settlements "will not be considered ordinary expenses for ratemaking purposes." The issue, however, is why this radical departure from longstanding precedent constitutes a justifiable approach, especially given its inconsistency with well-established public policy regarding settlements and its tendency to produce perverse economic incentives. The Commission has not addressed this more fundamental question.

[34] See, e.g., Williams v. First National Bank, 216 U.S. 582, 595 (1910); Gomez v. Brodhurst, 394 F.2d 465, 468 (3rd Cir. 1967) ("[V]oluntary settlements are to be encouraged"); Renfrew, "Negotiation and Judicial Scrutiny of Settlements in Civil and Criminal Antitrust Cases," 57 Chi. B. Rec. 130, 131 (1975) (federal judge describes encouragement of settlements as having "extraordinary importance"); Halper, "The Unsettling Problem of Settlement in Antitrust Damage Cases," 32 Antitrust L.J. 98, 100 (1966).

accounting treatment of settlements is especially tenuous given the fact that the only rationale offered by the Commission's Notice in support of this treatment is the purported need for consistency with a flawed blanket presumption of disallowance for adverse judgments.[35]

2. The Commission's Proposal to Include Pre-Judgment Settlements Above the Line Only to the Extent of the "Nuisance Value" Contradicts the Basic Premise of the Commission's Rules

The Commission seeks comment on whether it should readopt a ratemaking policy that "allows a carrier presumptively to include in its revenue requirement the 'nuisance value' of a lawsuit if a settlement is reached prior to judgment."[36] This rule directly contradicts the Commission's fundamental premise (which is itself flawed), namely that "it is the entry of a court decision that a law has been violated that drives our treatment of [these] costs."[37] Permitting above-the-line accounting for pre-judgment settlement costs only to the limited extent of nuisance value improperly treats settlements as tantamount to an adjudication of liability. Since pre-judgment settlements are arrived at independent of a "court decision that a law has been violated," any proposed limits on the presumptive allowance of settlement costs in a carrier's revenue requirement are unjustified, not

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[35] Notice at ¶ 11 (citing Litigation Costs Decision, 939 F.2d at 1046). See discussion at 11-12, supra.

[36] Notice at ¶ 12.

[37] Litigation Costs Order, 2 FCC Rcd. at 3248 ¶ 41.

only because settlement costs are ordinary and necessary expenses in the carrier's business, but also because such limits contradict the central proposition that undergirds the Commission's proposed rules. Accordingly, the Commission should affirm its current policy of allowing above-the-line accounting for all pre-judgment settlement costs.[38]

3. The Commission's Proposed Distinction Between Pre-Judgment and Post-Judgment Settlement Costs is Untenable

The Commission refuses to extend its proposed nuisance value exception to post-judgment settlements on the basis that, "when an adverse judgment has been entered by a court, the carrier should bear a heavier burden to 'show why ratepayers should bear any cost of a subsequent settlement."[39] As the Litigation Costs Decision found, however, the Commission's attempt to distinguish between pre- and post-judgment situations creates an incentive for a carrier to continue to litigate after an adverse judgment even if the cost of the appeal exceeds the amount for which the carrier could have settled post-judgment.[40]

In its Notice, the Commission nevertheless maintains this distinction because "the incentive to litigate that we would create by readopting the pre-judgment/post-judgment distinction is not so harmful to ratepayers that it warrants abandoning that

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[38] For the reasons discussed below, the Commission should continue to accord above-the-line treatment to all post-judgment settlements as well.

[39] Notice at ¶ 12 (internal citations omitted).

[40] Litigation Costs Decision, 939 F.2d at 1047.

distinction."[41] However, the Notice provides no objective support whatsoever for this conclusion.

While the Commission points out that ratepayers would be harmed only where the carrier ultimately prevails on appeal, it fails to cite any data to suggest that this is an infrequent occurrence. Indeed, as the overwhelming majority of commenters have well documented throughout these proceedings, an appeal from a judgment is a matter of right and judgments at trial are not infrequently reversed on appeal.[42] Seen in this light, the Commission's pre-judgment/post-judgment distinction not only encourages post-judgment litigation, but it also portends that in a significant number of cases substantially greater expenses will ultimately be borne by ratepayers than would have been the case had the Commission's framework encouraged (or at the very least been neutral to) post-judgment settlements.[43]

Nor may the Commission ignore other important public policy interests, such as the well-established policy favoring settlements which was discussed above. Many of the same considerations which impel settlements at the trial level are

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[41] Notice at ¶ 15.

[42] See, e.g., Comments of Section of Antitrust Law of the American Bar Association, filed in CC Docket No. 85-64.

[43] The increased incentive for post-judgment litigation arising from the Commission's pre-judgment/post-judgment distinction will have a significant adverse impact on parties other than ratepayers, as well, e.g., regulated carriers, the plaintiff who brought the suit and who now must incur additional costs at the appellate stage, the carrier's shareholders, and the judiciary.

also relevant to compromise at the appellate level, and no adverse inference can be drawn from the fact of settlement per se. Because the Commission's pre-judgment/post-judgment distinction is predicated on such an adverse inference, it is unjustifiable. At the very least, the Commission must square its proposed treatment of post-judgment settlement costs (and the attendant increase in post-judgment litigation) with longstanding judicial and regulatory policies which promote settlements and treat them as neutral acts, carrying no assumption at all, adverse or favorable, regarding the underlying merits of disputes.

Lastly, in addition to increasing carrier incentives to litigate after an adverse judgment, the Commission's proposed distinction will increase carrier incentives to settle prior to judgment, despite the dubious merit of an underlying complaint, so that at least litigation expenses (actual and expected) will be recorded above the line.[44] Given the fact that avoidance of such an excessive incentive to settle was the principal reason cited by the Commission for according similar treatment to adverse judgments and settlements of the same action,[45] the Commission can hardly justify a distinction within the settlement cost category which will produce the very same artificial incentive.

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[44] The Litigation Costs Decision points up this excessive incentive problem. See 939 F.2d at 1046.

[45] See Notice at ¶ 11.